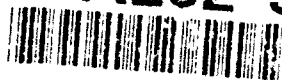


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# The Economic Impact of the Immigration of Soviet Jews to Israel

Mr.  
**James Vanderhoff**  
U. S. Department of State

*Faculty Research Advisor*  
Dr. Joseph E. Goldberg

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## **Introduction**

The immigration of a million Soviet Jews to Israel over the next three to five years is likely to have disastrous short-term effects on the Israeli economy. The long-term effects could prove to be a great blessing to the country or an unmitigated disaster. A favorable outcome will depend on how the Israeli government handles the absorption of the Soviet Jews; on making major changes to the nation's socialist economic policies and on changing its hard line stand regarding the occupied territories.

**Major Issues** - The issues concerning the immigration and resettlement of perhaps a million Jews from the former Soviet Union are numerous and affect every aspect of Israeli life. The issues, and the controversies surrounding them, have implications of economic, social and political natures.

**Social** - Israel, a nation of 4.5 million people, has opened its doors to more than a million Jews of the former Soviet Union who are fleeing both an increase in anti-Semitism and the collapse of the Soviet economy. This is consistent with the policy of the law of return which guarantees a home to any Jew wishing to immigrate to Israel. The very existence of the state of Israel is based in part on the safety it can provide for all Jews.

This influx of a million Soviet Jews could dramatically change the demographics of the Israeli state. For example—the immigration will help maintain the European orientation that Israel has held since prior to statehood by offsetting the high number of Sephardic births

among the Jewish population. Since religion was banned in the USSR for some 70 years, the Soviet Jews are secular with almost no religious background. This is seen by the orthodox Jews as a weakening of the Jewish religion in Israel. Depending on the political orientation of the immigrants, the Likud or Labor parties could gain a clear majority and break the political paralysis that has gripped the country in recent years.

Economic - While the potential long-term economic benefits of the influx of the Soviet Jews are tremendous, the near-term costs associated with the resettlement of a million penniless immigrants into a country of 4.5 million people are staggering. Israel's socialist economy is stagnant and in dire need of restructuring. Israel suffers from rising inflation and unemployment. Israeli experts estimate that as much as \$60 billion may be required to resettle the Soviet and Ethiopian Jews. Considering the state of the economy, there is no way Israel can raise the necessary funds without foreign assistance--mainly from the United States. The assistance was requested in the form of loan guarantees in the amount of \$10 billion.

Political - The controversy over the \$10 billion loan guarantees needed to resettle the Soviet and Ethiopian Jews has seriously strained Israel's relations with the United States, heretofore, her strongest supporter and ally. US-Israeli relations are probably at their worst since the Suez war in the 1950's. The US insistence that the \$10 billion not be used to settle immigrants in the occupied territories is seen as acknowledging the Arab position. The US sees Israel's continued building of settlements in the occupied territories as adversely

effecting the current peace talks. Both the Palestinians in Israel and the Arab neighbors outside her borders see the immigration as a threat, while the Israelis see it as a promise of greater security.

While all of the issues are intertwined and it is impossible to discuss one without relating it to the others, the primary focus of this paper will be on the economic issues related to the immigration of the Soviet Jews.

Aliyah - Immigration or "aliyah" as it is known in Hebrew, has been the life blood of the Jewish state of Israel, in fact, one of the most important purposes of the Jewish state is its promise of being a safe haven for any Jew. During the 40 odd years of its existence, Israel has enjoyed a steady trickle of Jewish immigrants from all over the world returning to their historic homeland.

Russian Jews - Russian Jews constituted a significant portion of Jewish immigration since 1897 until 1948 when severe restrictions were placed on Jewish emigration from the Soviet Union. Major changes in the former Soviet Union over the past few years have led to the lifting of the restrictions on Jewish emigration from the USSR, a rise in anti-Semitism and almost total economic collapse. These factors have all contributed to changing the trickle of immigrants into a deluge that threatens to swamp the country and its economy. It is estimated that upwards of 300,000 Soviet Jews have already arrived in Israel and the number is expected to grow to one million in the next three to five years.

## **The Soviet Jews - a Historical Perspective**

The two hundred-year history of the Jews in the Soviet Union has been fraught with discrimination, persecution, violence and even genocide. Prior to 1772, Jews were barred by law from living in, or even visiting, the Russian empire. When the Russians annexed eastern Poland they learned, much to their dismay, that the new territory included a large Jewish population. So as not to "infect" the rest of Russia, the Jews were confined to the Pale of Settlement--the 15 western provinces that had formerly been Lithuania and Poland. By the turn of the 19th century, 97 percent of Jews in Russia lived in the Pale. The numbers of Jews allowed in higher education and the professions were kept artificially low. They were barred from owning land and excluded from the heavy industries developing during the industrial revolution of the early 19th century. Jews were totally excluded from civil service and the officer corps and were limited to mercantile occupations and artisan's trades. In the mid-1800's, Emperor Alexander II eased the restrictions and allowed a small number of Jews having specific qualifications to live outside the Pale. By the end of the 1800's some five million Jews were living in the Russian empire.

Violence against the Jews began in earnest after the assassination of Alexander II. The new regime of Alexander III was especially hard on Jews, partly because of Alexander's personal hatred of the Jews, whom he blamed for the death of Christ, but also because of a wide-spread belief that Jews were responsible for the murder of Alexander II. The emperor named his brother governor-general of Moscow and ordered the expulsion of 20,000 Jews



from that city because his brother Sergei did not want to go to Moscow unless it was cleared of Jews.<sup>1</sup>

A press campaign against the Jews provoked waves of pogroms that hit the Jewish settlement in the 1880's. Pogroms erupted again around 1903-05 and finally from 1918-21. "Seeing in the revolution the realization of the Judeo-Masonic conspiracy and lacking the strength to repel the Bolsheviks, opponents of the regime vented their frustration on the Jewish population. Neither women nor the old or children were spared. Over a three-year period (1918-1920), no fewer than 200,000 Jews -- one-tenth of the then two million Jews in Russia -- were killed in pogroms alone."<sup>2</sup> Between 1881 and 1914, the beatings, murders and vandalism of Jews and their property had already caused some two million to flee to western Europe and North America. Of those who remained behind, a few gravitated towards revolutionary groups and were prominent in the Bolshevik party that came to power in October, 1917. The Bolsheviks ended the persecution of Jews and lifted the restrictive constraints they had lived under for generations. However, with this new found freedom came new restrictions. Along with all citizens of the Soviet Union, the Jews were restricted from practicing their religion.

The years following the Bolshevik revolution were some of the best in the history of Soviet Jewry. The Jews were offered educational and vocational opportunities unparalleled in their history. Considerable numbers of Jews filled the upper echelons of the party and state. Their higher level of education and literacy allowed them to fill the posts abandoned

by the Russian intelligentsia who had fled the revolution. Until the purges of the 1930's, Jews were also prominent in the secret police and the military. So drastic was the change from the lowest strata of Soviet life to the highest echelons that, to many Russians, it appeared that the Jews had taken over the country. This spark of anti-semitism was to be fanned in the years ahead.

The "good life" of the post-revolution years, as I have described it, was short lived and the years ahead held horrors unequaled in 4000 years of recorded Jewish history. During the Second World War, several hundred thousand Soviet Jewish soldiers died in combat against the Germans. In 1941, Hitler's army occupied the part of Russia that included the area that was once the Pale of Settlement. The area was still heavily populated by Jews and the Nazis systematically murdered an estimated 1.5 million of them (some believe with the cooperation and or help of the Russian people). The Germans reinforced the anti-Semitism held by the Russians by claiming that they had come to liberate the USSR from the "Judeo-Bolshevik" regime and that the Soviet Jews were to blame for the misfortunes of the war. Immediately after the war, Stalin accused Jews of disloyalty to the country and the regime and launched his infamous "anti-cosmopolitan" campaign. In 1948, Stalin closed all Jewish cultural institutions (schools, theaters, publishing houses etc.) in the Soviet Union. Jewish cultural and political leaders were arrested and exiled. Four years later, in 1952, the most prominent of them were shot. The following year, Russian anti-Semitism was once again rekindled when the Kremlin announced the "Doctors' Plot" which accused Jewish doctors of medically murdering prominent Soviet leaders. Many Russians

believed the story and avoided Jewish doctors and attacked Jews both verbally and physically. Life for the Soviet Jews after Stalin's death was to improve somewhat but as Zvi Gitelman points out many restrictions were still imposed:

After Stalin's death the most egregious forms of anti-Semitism were curbed, but Jews were permanently excluded from the upper echelons of the party and government, the directorships of important enterprises and research institutes, the foreign ministry, ministry of foreign trade, secret police, military academies and other "sensitive" positions. It became very difficult for Jews to enter the humanities or social sciences. The last channel of mobility for Jews was science and technology, which explains why such a high proportion of Jewish 'emigres are scientists, engineers and technicians.<sup>3</sup>

The Jews fared little better under Khrushchev who had an unwritten code restricting admission of Jews into higher education and prestigious professions. Under Brezhnev an ugly propaganda campaign against "Zionists" once again fanned the fires of anti-Semitism.

Anti-Semitism in the Soviet Union is more visible and blatant today than any time in the past forty years. It draws on both traditional Russian sources as well as sentiments evoked by the current radical changes in Soviet society. The glasnost, or openness, unleashed by President Mikhail Gorbachev has permitted suppressed anti-Semitic instincts to appear on the public agenda, and perestroika, or economic restructuring, has opened entrepreneurial opportunities that many Soviet citizens view with distrust and identify with Jews.<sup>3</sup>

For Soviet Jews, glasnost has proved to be a double edged sword. They are enjoying cultural and religious freedom heretofore unknown in the USSR but at the same time, "...The virulent and pervasive nature of the anti-Semitism that was brought to the surface by Glasnost is unprecedented in the seventy year period of Communist rule."<sup>4</sup> It is difficult for us in the west, where our freedoms are protected by law, to fathom that in the 1990's Soviet Jews, once again, fear for their lives. Over the past few years, thousands of leaflets have

been distributed in the Soviet Union calling for pogroms against the Jews, going so far as to specify dates. While the pogroms have not occurred, the warnings have struck terror in the hearts of many Soviet Jews. In recent years ultra-nationalist groups, such as the infamous "Pamyat", have gained prominence in the Soviet Union and enjoy considerable grass roots support. Their rhetoric is fearfully reminiscent of the Nazis prior to the holocaust. In a four-day convention of hundreds of delegates from all over the USSR, speeches voiced the commonly accepted belief that most of Russia's problems in this century are attributed to the Jews. They also demanded that all Jews be stopped from leaving the USSR until the degree of guilt of every Jew be examined by a "tribunal of the Russian people" and the guilty among them stand trial for the "crimes" they have perpetrated against Russia. Recent polls in the Soviet Union showed that more than a quarter of the population of Moscow share anti-Semitic prejudices, some 8.8 percent believe that Jews must be punished for crucifying Christ, and 7.6 percent think that Jews are responsible for the Bolshevik terror. The Jewish Cultural Association reports that no fewer than 1,000 anti-Semitic demonstrations had taken place in the Soviet Union in 1989.<sup>2</sup> Very little has been done by the government to repress anti-Semitism in the USSR. In fact, many prominent government officials are openly anti-Semitic. One example is Alexander Sukharev who was co-author of the introduction to an anti-Zionist publication called simply the "White Book". At the time, Sukharev was the first vice president of the Association of Soviet Lawyers and shortly after the book was published was appointed Procurator-general of the Soviet Union! Two hundred members of the Congress of People's Deputies signed a petition asking Gorbachev to publicly condemn antisemitism. The petition was not granted.

If the security of Jews was in serious question under a strong central government, how much more serious is the situation with the disintegration of the Soviet Union? Will the rampant ethnic violence in Yugoslavia be repeated in the former Soviet republics with the Jews as the targets? With the horrors of the holocaust fresh in their memories, hundreds of thousands of Soviet Jews have decided to learn the answer to these questions from within the relatively safe borders of Israel.

## **The Problems of Absorption**

Housing and Jobs - The absorption of the one million plus immigrants is an immense undertaking. The most difficult tasks are providing housing and creating jobs for the refugees, most of whom arrive in Israel with no assets and look to the government as their sole means of support. To provide an analogy from an American perspective--it would be the equivalent of the U.S. government providing housing and jobs for 60 million penniless immigrants arriving in the United States over a 3-5 year period. It is doubtful that even the United States, with one of the strongest economies in the world, could absorb this proportional number of immigrants without bankrupting the nation. It is even more doubtful that Israel will be able to accomplish this task without considerable economic assistance in the short-term and major economic reform in the long-term.

Unlike the United States, who would never allow itself to get into a position of trying to absorb such a vast quantity of immigrants, Israel has no choice. The "Law of Return"

grants citizenship to any Jew wishing to immigrate to Israel. The Jews of the former Soviet Union have been arriving in droves. Driven by rising anti-Semitism and the collapse of the Soviet economy, they left the Soviet Union in panic, not knowing when, or if, the exit door would once again slam shut. Ironically, the flood slowed considerably in 1991 when tens of thousands of potential immigrants in the Soviet Union were advised by friends and family, already in Israel, to wait until the conditions improved. Israel is already suffering from acute housing shortages and record unemployment especially among the recent arrivals.

The Israeli government's attempts to deal with this massive flood of immigrants has been inadequate. According to Mikhail Kleiner, the head of parliament's Absorption Committee, a solution to the problem of absorption exists but it would be politically impossible to apply. "If the government was to do what has to be done to absorb the immigrants properly, it would have to make decisions that would cost the Likud political office. It would have to cut services to Israelis by 25 percent and raise taxes by 25 percent. And it is not going to do that."<sup>5</sup>

In all fairness, the number of immigrants is far greater than anyone could have anticipated. However, many of the efforts taken thus far have been mis-directed. For example, most of the housing being built for the immigrants is not in the areas that they choose to live. The Washington Post reports, "According to the government, 29 percent of housing construction for immigrants has been in the Negev region, but only 7 percent of the immigrants have moved there; 49 percent of new immigrants are living in greater Tel Aviv,

but only 22 percent of the new housing is there. Meanwhile, housing officials say that at least 21,000 housing units have been built or are under construction in the occupied territories and at least 14,000 in East Jerusalem."<sup>6</sup> It should be noted that according to most reports only about one percent of the immigrants have moved to the occupied territories where most of the housing construction has taken place.

The Shamir government had originally planned to provide housing and jobs through free-market methods within the private sector but when reforms in labor laws, capital markets and trade ran into opposition from the Histadrut (Israel's labor federation) and left-wing legislators, Shamir effectively gave up. He handed over control of immigration and housing to Ariel Sharon who abandoned the free-market methods and began a \$2.5 billion centrally planned housing construction program. Sharon, with his own political agenda, sought to use the immigrants to strengthen Israel's control over strategic territories including the occupied areas. When the experts pointed out that most of the Soviets were highly educated professionals and urbanites and would probably not settle in the outlying areas, Sharon pressed ahead with plans to build more than half of the 90,000 government financed dwellings there. When private and foreign contractors balked at building outside central Israel, afraid that they would be unable to sell the homes, Sharon won approval of a program where the state would buy any housing units in unprofitable areas that the contractors were unable to sell.

It would seem that the experts and contractors were right as in August, 1991, Deputy Budget Director, Amnon Safran predicted to a parliamentary committee that the state would have to spend \$860 million next year buying empty apartments in frontier areas from contractors unable to sell them. <sup>7</sup>

Loan Guarantees - The cornerstone of the Israeli plan for absorbing the influx of Soviet Jews is the controversial \$10 billion loan guarantees that Yitzhak Shamir has requested from the US government. Not loans themselves, the guarantees would allow the Israelis to borrow the \$10 billion on the world market at favorable interest rates. The Bush administration has requested that Congress delay the guarantees as they believed that they would adversely effect the peace talks and insist that the money not be used to build settlements in the occupied territories.

Although most of the controversy surrounding the loan guarantees concerns the settlement of the immigrants in the occupied territories, my focus will be an economic one-- Israel's inability to repay the \$10 billion loans and what it may eventually cost the US taxpayer.

The proponents of the deal say that it will cost nothing because the US would pay only if Israel defaults and Israel's record on loan payments has been excellent. The opponents say that the guarantees will cost, at a minimum, hundreds of millions of dollars



because a certain percentage must be held in escrow. As a maximum, they claim that it will cost the US the full \$10 billion plus interest.

Frank Collins, a free-lance journalist, writing for The Washington Report on Middle East Affairs, argues that, "The proposed support for Israel in each of the next five years includes the existing approximately \$4 billion per year in grants and other aid plus the demanded \$2 billion in loan guarantees. Scaled up by the ratio of the gross national products of the United States and Israel, if the loan guarantees were to be granted, the total support level for the next five years would be equivalent to roughly \$3 trillion, nearly equal to the national debt of \$3.5 trillion of the United States."<sup>8</sup>

Collins goes on to argue that Israel's existing foreign debt is \$16.9 billion with interest of about \$1.5 billion per year. He estimates that the interest on the \$10 billion would raise the total interest payments to some \$2.35 billion a year. He asks his readers to consider the enormity of a debt of \$10 billion plus accumulated interest of \$19.3 billion to a country as small as Israel with a population of only 5 million. He estimates that the debt represents \$5,860 for every citizen and \$23,440 for a family of four. Collins sums up his opposition to the loan guarantees by saying, "Only the wildest dreams of Israeli population and GNP growth could lead to conclusions other than the inevitability of default."

Dr. Israel Shahak, the chairman of the Israeli League of Human and Civil Rights, lends support to Collins' argument in the Hebrew Press. In his article, he quotes Israeli economist Zvi Timor--"For years we have been repaying all our debts from what we've been

receiving as American aid. Each year Israel gets \$1.3 billion of economic aid, of which \$1.1 billion goes for debt repayment."

Shahak goes on to argue that in order to repay the loans Israel would have to increase its exports by at least \$4 billion or some 43% in a single year--a possibility that both Shakak and Timor recognize as absolutely impossible. He once again refers to Timor when he states, "Timor is right in pointing out that without the US Guarantees, "a state like Israel, which already has an enormous foreign debt per capita, enormous defense budget, enormous budgetary deficit and quite sizable trade deficit, would not be considered an attractive borrower on the international financial market". It can be mentioned in passing that an Israeli budgetary deficit exists when the not-yet granted American guarantees are already counted on the revenue side! All these facts only reinforce disbelief in Israel's ability to ever repay the loans guaranteed by the US."<sup>9</sup>

The publication in which both articles appeared, has a very strong pro-Arab and anti-Israel slant. The tone of each article was also rather anti-Israel, however, the figures they cite regarding Israel's existing debt and use of American aid to pay the interest on the debt, were substantiated in numerous other articles. I found further support for their argument in an editorial in the much more neutral Wall Street Journal written by a vice president of Dow Jones & Co. Her argument is quoted in part:

...It's hard to imagine a rational economic argument for any loan, much less one at lower than market interest rates, for the settlement of refugees in dangerous and disputed territory that may not remain in Israel's hands at the end of (the) peace process. In short, no sensible banker would guarantee a

loan to build a house on a lot claimed by a hostile next-door neighbor. Israel, of course, argues that the \$10 billion it seeks to borrow with US guarantees isn't earmarked for West Bank settlements. But, as any banker or borrower knows, money is fungible. ...loans have a way of becoming grants. From 1974 to 1989, Israel received some \$16.4 billion in loans that the US converted to grants, according to congressional researchers cited in a Journal news article last week. ...why, in a world witnessing the rapid collapse of socialist economics, American taxpayers should subsidize with loan guarantees the perpetuation of Israel's faltering, socialist economic policies?"<sup>10</sup>

While these are the views of only three people, there is widespread agreement that the Israeli economy is in serious trouble and in dire need of reform.

The opponents of the \$10 billion guarantees, argue that Israel will not be able to repay the loans guaranteed by the US. The economic picture looks even worse when you consider that the \$10 billion is only a fraction of the amount needed to resettle a million Soviet Jews. Israeli government planners calculated that they would need \$60-70 billion to deal with the influx. They expect to obtain more than half from tax revenues, domestic borrowing and the sale of government-owned businesses. That still leaves \$25-30 billion to be raised outside Israel. This is no small matter when you consider that a third of the country's national budget is already devoted to repaying existing debts. The only way Israel can raise the billions needed to resettle the Soviet Jews, without bankrupting the country, is through massive economic growth brought about by a total revamping of Israel's socialist economic system.

## **The Israeli Economy**

The Israeli economy is a shambles. Forty years of socialism have led to the same inefficiencies and waste that ultimately undermined socialism in Eastern Europe. The only thing that has saved Israel from complete economic collapse is foreign aid, the majority of which has come from the United States. Foreign aid has allowed Israeli politicians to avoid the consequences of their actions, to indulge themselves in inefficient economic policies and to put off the day of reckoning for decades. Such politicians have not done the Israeli people any favors. They have systematically eroded private property, free exchange, entrepreneurship, and Israel's economic incentives, to the point where even the country's security is at risk. "

This view of the Israeli socialist system, expressed by Bruce Bartlett, an economist with the US Treasury Department, is shared by hundreds of experts both inside and outside of Israel. In fact many of Israel's leaders have recognized the need for economic reform but have been unwilling or unable to effect any meaningful changes. Attempting to make radical changes in the socialist programs in Israel would be analogous to a US politician making drastic cuts to social security benefits. The result would be political suicide.

The history of socialism in Israel is older than the state itself. Two of the oldest and most influential bodies in Israel are the Jewish Agency and the Histadrut--Israel's labor federation. The British granted the Jewish Agency the power to act as a quasi-government on behalf of the Palestinian Jews following World War I. In 1921 the League of Nations recognized the agency as a political body representing the Jews of Palestine. The agency became the conduit for all Jewish economic aid.

The Histadrut also had quasi-governmental powers related to medical care, education and other social services. After independence in 1948, these two bodies continued to wield considerable influence and are responsible for much of the economic policy that exists today.

The Histadrut could very well be the most powerful body in Israel. It is closely allied with the Labor Party and owns an incredible 25 percent of the country's enterprises and employs 16 percent of the labor force.<sup>12</sup> These enterprises generate approximately 20 percent of the GNP. According to Bartlett, these enterprises are poorly run and most lose money. He cites Koor Industries, Israel's largest company, which was founded by the Histadrut. Poor management practices in the company led to a major government bail-out of the company out in 1989. Lack of reforms within the company have led to continued losses and the threat of bankruptcy.

The Histadrut has the power to effectively block any economic reform that it opposes. For example, it blocked Finance Minister Yitzhak Modai's proposal to delink minimum wages from automatic cost-of-living increases and also permitting night-shift work without bonuses, a move that would have allowed factories to hire new workers quickly. They effectively blocked the privatization of the profitable state-owned Israel Chemicals Company by convincing the workers that they might lose their jobs if new foreign owners took over.

A New York Times article provides insight into the power of the Histadrut:

Israel's national trade union all but shut the nation down today with a general strike protesting the Government's plan to tax Israelis to pay for the absorption of Soviet immigrants.

The Histadrut union, which represents workers in virtually all areas of public and private enterprise, shut down radio, television, air traffic, telecommunications, government offices, banks, most schools, postal and port services. It put a number of other fields, including health services, on holiday schedules.

Ignoring a court order last week requiring Histadrut workers to remain on the job, the union threatened to continue the strike indefinitely, until the Government reversed or modified its decision last week to raise taxes, lower the minimum wage and carry out other economic steps to pay for the resettlement of immigrants.<sup>13</sup>

According to Diehl Jackson writing for the Washington Post, when the massive influx of Soviet Jews began in 1989, Israeli government economists, as well as financial experts from both the US and Europe, warned Shamir that the only way Israel could absorb the influx was to open its markets to private and foreign investment and dismantle the quasi-socialist system that gives it one of the most state-controlled economies outside the dwindling Communist world. This advise apparently fell on deaf ears as the Shamir government has responded to the influx in classic socialist fashion by launching massive, state-run housing and job programs.

Because the Shamir government has built so much of the immigrant housing in areas where private entrepreneurs are reluctant to invest, the government will have to create thousands of needed jobs largely through make-work programs. To this end, Finance

Minister Yitzhak Modai has proposed a \$3.6 billion jobs plan for 1992 under which the government would subsidize the salaries of thousands of extra workers in the construction industry, state-owned factories, scientific institutes and even archaeological digs. State firms are to be induced to hire up to 20,000 new employees as trainees, whether they need them or not!

Israeli economists, including some senior officials of the central bank, say the massive state-directed employment policy will merely propel the country deeper into the morass of central planning and socialism that most of the rest of the world is abandoning. "The Israeli vision of the future is to continue down the same failed, dismal path of more and bigger government," economist Alvin Rabushka charged in a recent study.<sup>14</sup>

The Israeli budget deficit has been running at 4 percent of the GNP but was expected to rise to 6 percent in the 1992 budget. Inflation had been hovering around 20 percent but was nearing 30 percent last October. The International Monetary Fund warned last July that any increase in inflation could be the beginning of an upward spiral.

There is genuine concern that Israel could return to the hyper-inflation of the 1980's. The inflation rate was 500 percent in 1985 when George Shultz of the Reagan administration, with the help of \$1.5 billion in additional aid, persuaded the Likud-Labor coalition government to adopt a inflation stabilization program.<sup>12</sup>

On January 10, 1990, Mary Curtius of the Boston Globe, reporting on the Israeli economy referred to recent figures showing nearly half the nation lives below the poverty line.

The Absorption Process - For many Soviet Jews, the first few days or weeks living in Israel is probably a dream come true. Not only are they given relatively large sums of money, they are confronted with stores overflowing with consumer products only dreamed about in the Soviet Union. It probably takes several weeks or months for the harsh reality to set in. The reality is acute housing shortages, skyrocketing rents, rampant unemployment especially among the immigrants and double digit inflation. Even given these problems, they probably have it better than most immigrants anywhere in the world. "A family of three receives about \$11,000 for the first year, plus free medical expenses for six months, and free language and job training. They also receive loans for mortgages and are exempt from income tax for one year. After the first year, the funds decline. Thus, the first year rental allowance of \$4,000, included in the \$11,000, declines in the second year to about \$2,500; and in the third year, to \$1,800. Soviet Jews thus need to be at least partially self-supporting to pay the rent after the first year."<sup>15</sup>

Not only are many immigrants still unemployed after the end of their first year, the government has been forced to reduce the subsidies and services provided to them. After the most recent cuts, instead of receiving \$11,000, the immigrants now receive a grant of \$4,250 and a loan of \$2,500 payable beginning three years later. Because of the housing shortage in Israel, a typical one-bedroom apartment in most cities rents for about \$450 per month which equates to \$5,400 a year or about 80 percent of the immigrants' first year subsidy.<sup>16</sup>



There is considerable concern within Israel that the housing and job shortages will dry up the flood of immigrants. There is also the concern of emigration of the Soviets to the US or other countries--or for that matter--back to the USSR. " Michael Bruno, former governor of the Bank of Israel, warns that unless the government moves quickly to reform the economy, unemployment, which has already hit 11 percent, could reach as high as 18 percent, with more than 200,000 people leaving Israel in search of better opportunities." <sup>17</sup>

Israel's homeless - The absorption of the immigrants is having a serious detrimental effect on another sector of the population. Landlords taking advantage of the subsidies given to the immigrants have doubled and tripled rents and are demanding--and receiving--a full year's rent in advance. The segments of the population most effected by the housing shortage are not the immigrants but the young Israeli couples and poor Israeli families. Unable to pay the higher rents demanded by the landlords, thousands of evicted Israelis have erected small tent cities in various locations throughout Israel. Back in July of 1990, 70 of the homeless near Tel Aviv, fed up with their situation, barricaded themselves on a roof, hurled molotov cocktails down into the street and threatened mass suicide until Minister of Housing, Ariel Sharon, promised to listen to their demands and pay a visit to their tent city. According to an article in the July 26, 1991 Christian Science Monitor, Israel's Finance Minister estimates that more than 70,000 people will be homeless by March, 1992.

Blessing or Burden? - The Soviet Jews that are immigrating to Israel are possibly the richest talent pool ever to immigrate, as a group, to any country in history. This is

particularly significant to Israel as the group will make up as much as 20-25 percent of the entire population. According to many reports, more than 50 percent of the Immigrants have advanced academic degrees (scientists, engineers, computer programmers, doctors); more than 20 percent are from the service sector (nurses, tailors, drivers etc.) and only 14 percent are estimated to be blue collar workers. Strobe Talbott of Time describes this talent pool and the problems associated with it when he says, "...they are rich in education, skill and ambition. Already there are enough doctors for a clinic on every corner, enough musicians for a string quartet in every apartment building and enough engineers and computer programmers for a booming, high-tech export-oriented manufacturing sector on the order of Taiwan's or Singapore's.... Yet Israel is too burdened by defense spending and too isolated internationally, especially in its own region, to take advantage of the infusion of human capital that the Soviet Jews represent." He sums up his argument by saying that Israel must choose between having Arab lands or Arab markets. It can either absorb the West Bank or the Soviet Jews.<sup>18</sup>

Reforms - There has been considerable rhetoric but little action taken on economic reform. In fact, the actions taken thus far in the absorption process have resulted in more social welfare programs and more government intervention.

According to Louise Lief and David Makovsky of US News and World Report, Israel has made considerable progress in economic reforms since 1985, by "...removing almost all the deeply-entrenched government subsidies, reducing defense spending's share of Israel's GNP,

loosening foreign-currency controls for Israeli businesses and withdrawing the government from capital markets." While some progress has been made, it is obvious that the country has a long way to go to achieve a free market economy. The US News report goes on to say that the state employs some 39 percent of the labor force, accounts for 20 percent of industrial production and has stalled for years on privatizing 150 state owned companies. At the urging of the US government and American Jewish leaders, Shamir recently created a panel to overrule the ministers who have paralyzed the privatization process. The panel, thus far, has been unsuccessful.<sup>12</sup>

Some reports are far less critical of Israel's efforts to reform their economic policies and stimulate growth. Recognizing the rich talents of the immigrants and the fact that the Israeli work force is one of the best educated and most highly skilled in the world, the government is betting on the high-tech industry as their salvation.

Leland Montgomery, writing in Financial World reports:

Especially since last September, the government has done everything in its power to make Israel a more attractive place for high-tech investment. The weapons it has brought to bear are a powerful mix of outright grants, R&D tax credits and subsidies for wage and training costs.

A company bringing in new capital equipment, for example can get a grant for up to 38% of the cost. R&D projects get up to 66% of their expenses reimbursed. And the government will pay up to one half of the wages for any immigrant for the first six months of employment. These incentives are strongly weighted towards the R&D end of the spectrum.<sup>19</sup>

Montgomery reports that the incentives are working. In the last six months the government has approved applications for \$800 million in plant extensions or start-ups. Some of the more notable companies investing include: Microsoft, Intel, Motorola and Sara Lee. This new investment represents the potential of creating some 15,000 jobs. The problem of high-tech industry is that it does not employ a lot of people and high-tech positions are expensive to create. 15,000 jobs are less than a drop in the bucket when more than that number of immigrants arrive every month.

In a Wall Street Journal article on the need for economic reform in Israel, Daniel Doron and Yuri Shtern call for a reduction of government regulation of the economy which they say controls everything from the size of a doughnut to the rate of interest. They point out the need for sharply lower taxes and the reformation of capital markets to allow private capital formation and the launching of new businesses.

Doron and Shtern contend that the housing problems could be eased if the government would release some of the land it holds at non-monopolistic prices (the government or the Jewish National Fund hold 93 percent of the land in Israel). Further, they recommend the elimination of the rigidities and monopolies in the building trade, reducing taxes on building materials and cutting the bureaucracy that makes getting a building permit a nightmare.

Doron and Shtern sum up their argument this way:

These are only a few of the steps that can be taken to create a productive and competitive economy without which immigrant absorption will falter. Neither

additional government allocations nor increased charitable contributions from abroad will suffice to provide housing and professional employment for the forthcoming masses of well-educated Soviet Jewish immigrants.

A structural reform encouraging private initiative and creating economic growth, rather than redistributing existing resources, will enable Israel to absorb immigrants and to take advantage of the enormous human capital they represent.<sup>20</sup>

## **Conclusion**

The Soviet Jews represent the greatest untapped resource in Israel today. In order to use this resource, the Israeli government must absorb the immigrants and provide meaningful employment for them. Thus far, the government's record in the absorption process has been poor at best. To quote Yonatan Livni, a lawyer who assists Soviet immigrants with day-to-day legal problems: "Absorption is happening despite the government, not because of it."

The Christian Science Monitor reports that the absorption effort is made more difficult by constant "spats" among government officials responsible for the immigrants. "For a while, earlier this year, Housing Minister Ariel Sharon would not speak to Absorption Minister Yitzhak Peretz, while feuding ministers boycotted the "aliyah" Inner Cabinet meetings."

Unemployment among the Soviet immigrants is running at about 40 percent. Most who have found work, are working outside their profession. It is quite common to find highly trained professionals with advanced degrees, sweeping streets, waiting tables and

pumping gas. Although many of the immigrants are "professionals" and have advanced degrees, most do not demonstrate the same level of expertise as professionals trained in the west. It is therefore necessary to retrain many professionals to bring them up to western standards.

Israeli leaders have failed, thus far, to make the bold, sweeping, comprehensive economic reforms, needed to turn the Israeli economy around. The government privatization plan is to sell 20 percent of its holdings in the Zim Navigation Company, 23 percent in the Bezeq Israel Telecommunications Corp., 26 percent of Maman Cargo Terminal and Handling Ltd., and all shares in Malam System Ltd., Agridev Ltd., and Dead Sea Periclase Ltd. The government needs to get serious and sell 100 percent of their holdings and stop shoring up these poorly managed companies. They need to make bold moves to attract foreign investment such as reducing the 42 percent corporate tax level. They need to streamline the bureaucratic process. The Atari Corporation recently canceled plans to build a \$150 million plant and a \$75 million investment center in Israel because of excessive government delays in approving their proposals.<sup>17</sup>

Until the government gets serious about economic reforms, the economy is likely to remain stagnant. Israeli leaders are not likely to make the difficult and unpopular changes to the economic policy as long as the US continues to provide massive amounts of unconditional foreign aid. If the Bush administration were to link future foreign aid packages and the \$10 billion loan guarantees to specific economic reforms, it would force

Israeli leaders to make necessary changes and, at the same time, allow them to do so without committing political suicide.

Israel already enjoys very favorable trade agreements with the US and the European Community. A real and lasting peace with its Arab neighbors could provide Israel with a new market of some 60 million people within a short distance of its borders. This market coupled with the enormous potential of the Soviet Jews could be the salvation of the Israeli economy. Although, the Shamir government has made it clear that they are not willing to relinquish one inch of occupied territory, according to the Los Angeles Times, opinion polls consistently show that, contrary to their government representatives, most Israelis are ready to consider territorial concessions as part of a comprehensive peace agreement. Why not expand the concept of "land for peace" to "land for peace and free trade"? Return of the disputed lands should be linked to total elimination of the Arab boycott and open markets. When countries develop a strong interdependence based on trade, hostilities based on ideology tend to be eliminated.

Who, at the end of World War Two, could have imagined the close relationship that exists today between the US and Japan and the US and Germany? Who could have imagined, even three years ago, that the 40 year cold war would abruptly end and that we would become friends, albeit cautious ones, with the USSR? Is it therefore so difficult to imagine peace and economic interdependence between Israel and its Arab neighbors?

The end of the cold war has allowed the US to cut its defense budget by some 30 percent. The end of hostilities with its Arab neighbors would allow Israel to make similar cuts to its huge defense budget. If the US and the UN were to guarantee the safety and security of Israel, these cuts could be made with a greater degree of confidence.

Peace and economic ties with its Arab neighbors could be the first step on the road to economic independence for the State of Israel and a solution to many of the immigration issues. It is time for Israel to come to the peace table with US and UN backing, ready to negotiate land for peace and economic treaties.



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